Big Banks Take Huge Stakes in Aluminum, Petroleum and Other Physical Markets, then Manipulate their Prices

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Giant Banks Take Over Real Economy As Well As Financial System … Enabling Manipulation On a Vast Scale

Top economists, financial experts and bankers say that the big banks are too large … and their very size is threatening the economy. They say we need to break up the big banks to stabilize the economy. They say that too much interconnectedness leads to financial instability.

But – as shown below – the big banks are getting bigger and bigger … and getting into ever more interconnected markets.

Indeed, big banks aren't even really *acting* like banks anymore. Big banks do very little traditional banking, since most of their business is from financial speculation. For example, we noted in 2010 that less than 10% of Bank of America's assets come from traditional banking deposits.

The big banks are manipulating every market. They're also taking over important aspects of the *physical* economy, including uranium mining, petroleum products, aluminum, ownership and operation of airports, toll roads, ports, and electricity.

And they are using these physical assets to massively manipulate commodities prices … scalping consumers of many *billions of dollars* each year. More from Matt Taibbi, FDL and Elizabeth Warren.

A 2-year bipartisan probe by the Senate Permanent Subcommittee on Investigations has shined a light on this problem, culminating in a new 400-page report.

Senator Levin – the Chair of Subcommittee – summarizes the findings from the investigation:

> "Wall Street's massive involvement in physical commodities puts our economy, our manufacturers and the integrity of our markets at risk," said Sen. Carl Levin, D-Mich., the subcommittee's chairman. "It's time to restore the separation between banking and commerce and to prevent Wall Street from using nonpublic information to profit at the expense of industry and consumers."
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> "Banks have been involved in the trade and ownership of physical commodities

for a number of years, but have recently increased their participation in new ways," said Sen. John McCain, R-Ariz. "This subcommittee's hearing is an opportunity to examine that involvement, determine whether it gives rise to excessive risk, and identify potential causes for concern that warrant further oversight by Congress and financial regulators."

One focus for the subcommittee is the management of Detroit-area metal warehouses run by Metro Trade Services International, the largest U.S. warehouse company certified to store aluminum warranted by the London Metal Exchange for use in settling trades. Since Goldman bought Metro in 2010, Metro warehouses have accumulated up to 85 percent of the U.S. LME aluminum storage market.

Since Goldman took over the warehouses, the wait to withdraw LME-warranted metal has increased from about 40 days to more than 600 days, reducing aluminum availability and tripling the regional premium for storage and delivery costs.

The investigation revealed a number of previously unknown details about these deals: that Goldman's warehouse company paid metal owners to engage in "merry-go-round" deals that shuttled metal from building to building without actually shipping aluminum out of Metro's system; that the deals were approved by Metro's board, which consisted entirely of Goldman employees; and that a Metro executive raised concerns internally about the appropriateness of such "queue management."

Goldman didn't just store aluminum; it was involved in massive trades of aluminum at the same time its warehouse operations were affecting aluminum availability, storage costs, and prices. After Goldman bought Metro, it accumulated massive aluminum holdings of its own, and in 2012, added about 300,000 metric tons of its own aluminum to the exit queue at its warehouses.

The Subcommittee investigation also examined other instances of Wall Street bank involvement with physical commodities. The Subcommittee report details how JPMorgan amassed physical commodity holdings equal to nearly 12 percent of its Tier 1 capital, while telling regulators its holdings were far smaller; and that at one point it owned an amount equal to more than half the aluminum used in North America in a year. The report also discloses that, until recently, Morgan Stanley controlled 55 million barrels of oil storage capacity, 100 oil tankers, and 6,000 miles of pipeline, while also working to build its own compressed natural gas facility and supply major airlines with jet fuel.

Details are also provided about Goldman's ownership of a uranium trading company and two open pit coal mines in Colombia. When one of the mines was shut down last year due to labor unrest, Goldman's Colombian subsidiary requested military and police assistance to end a human blockade — before paying the miners with $10,000 checks to end the protest.

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The findings and recommendations from the bipartisan report are as follows:

Findings of Fact

(1) Engaging in Risky Activities. Since 2008, Goldman Sachs, JPMorgan Chase, and Morgan Stanley have engaged in many billions of dollars of risky physical commodity activities, owning or controlling, not only vast inventories of physical commodities like crude oil, jet fuel, heating oil, natural gas, copper, aluminum, and uranium, but also related businesses, including power plants,

> coal mines, natural gas facilities, and oil and gas pipelines.
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> (2) Mixing Banking and Commerce. From 2008 to 2014, Goldman, JPMorgan, and Morgan Stanley engaged in physical commodity activities that mixed banking and commerce, benefiting from lower borrowing costs and lower capital to debt ratios compared to nonbank companies.
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> (3) Affecting Prices. At times, some of the financial holding companies used or contemplated using physical commodity activities, such as electricity bidding strategies, merry-go-round trades, or a proposed exchange traded fund backed by physical copper, that had the effect or potential effect of manipulating or influencing commodity prices.
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> (4) Gaining Trading Advantages. Exercising control over vast physical commodity activities gave Goldman, JPMorgan, and Morgan Stanley access to commercially valuable, non-public information that could have provided advantages in their trading activities.
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> (5) Incurring New Bank Risks. Due to their physical commodity activities, Goldman, JPMorgan, and Morgan Stanley incurred multiple risks normally absent from banking, including operational, environmental, and catastrophic event risks, made worse by the transitory nature of their investments.
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> (6) Incurring New Systemic Risks. Due to their physical commodity activities, Goldman, JPMorgan, and Morgan Stanley incurred increased financial, operational, and catastrophic event risks, faced accusations of unfair trading advantages, conflicts of interest, and market manipulation, and intensified problems with being too big to manage or regulate, introducing new systemic risks into the U.S. financial system.
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> (7) Using Ineffective Size Limits. Prudential safeguards limiting the size of physical commodity activities are riddled with exclusions and applied in an uncoordinated, incoherent, and ineffective fashion, allowing JPMorgan, for example, to hold physical commodities with a market value of $17.4 billion – nearly 12% of its Tier 1 capital – while at the same time calculating the market value of its physical commodity holdings for purposes of complying with the Federal Reserve limit at just $6.6 billion.
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> (8) Lacking Key Information. Federal regulators and the public currently lack key information about financial holding companies' physical commodities activities to form an accurate understanding of the nature and extent of those activities and to protect the markets.

Of course, the Federal Reserve – instead of regulating the banks, encouraged them to buy all of these physical assets. As Reuters notes:

> [The Senate report] also points the finger at the Federal Reserve, saying the central bank has taken insufficient steps to address the risks taken by financial holding companies gathering physical commodities. The Fed in some cases was unaware of the growing risk, the report said.

Pam Martens points out:

> Adding to the hubris of the situation, the Wall Street banks' own regulator, the Federal Reserve, gave its blessing to this unprecedented and dangerous encroachment by banking interests into industrial commodity ownership and

has effectively looked the other way as the banks moved into industrial commerce activities like owning pipelines and power plants.

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One would think that the mega banks' regulator, the Federal Reserve, would be the first line of defense against this type of dangerous sprawl by banks. According to the Levin Subcommittee report, the Federal Reserve was actually the facilitator of the sprawl by the banks. The report notes:

> "Without the complementary orders and letters issued by the Federal Reserve, many of those physical commodity activities would not otherwise have been permissible 'financial' activities under federal banking law. By issuing those complementary orders, the Federal Reserve directly facilitated the expansion of financial holding companies into new physical commodity activities."

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